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DIRECTORATE OF INTELLIGENCE

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Prospects for South Korean Defense Spending

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Summary

We believe that South Korea remains committed to allocating a fixed percent of gross national product (GNP) to defense. Nonetheless, a change in the method of calculating GNP will leave the ratio below the 6-percent level in 1985, and budget austerity over the next year or two will complicate prospects for a near-term return to the 6-percent level.

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South Korea's failure to reach 6 percent of GNP for defense over the last two years results primarily from a recomputation of national accounts in accordance with recommendations of the International Monetary Fund. The use of more sophisticated data collection methods, as well as the inclusion of some new industries and economic activities, in fact produces significantly higher GNP estimates for the past ten years. Measured against these new estimates, defense spending has surpassed 6 percent of GNP only in 1980, 1981, and 1982. (See table for a comparison of adjusted rates of defense spending.)

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Unexpectedly strong growth in 1983 and 1984 also pushed the ratio down as nominal GNP in both years surpassed estimates made when defense plans were formulated.

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This memorandum was prepared by [redacted] Korea Branch, Northeast Asia Division, Office of East Asian Analysis. Comments and queries are welcome and may be addressed to Chief, Korea Branch [redacted]. Information available as of 10 October has been incorporated.

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The 1985 Debate

In planning defense expenditures for 1985, the South Korean Government was concerned that allocating 6 percent of GNP under the new accounting ground rules would require a boost of better than \$500 million in expenditures. Such an increase for an economy with an estimated \$79 billion GNP and a \$13 billion national budget would necessitate sharply reduced outlays in nondefense areas. Moreover, critical economic stabilization measures entailed in Seoul's commitment under a standby agreement with the International Monetary Fund would have to be sacrificed. [redacted]

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Deputy Prime Minister Shin Byong Hyon in talks with US officials has emphasized that no one in Seoul questions South Korea's commitment -- conveyed verbally by the late President Pak Chung Hee in 1979 -- to stand by the 6-percent spending goal. He has also suggested that Seoul will again attain the 6-percent level, perhaps as early as 1986. [redacted]

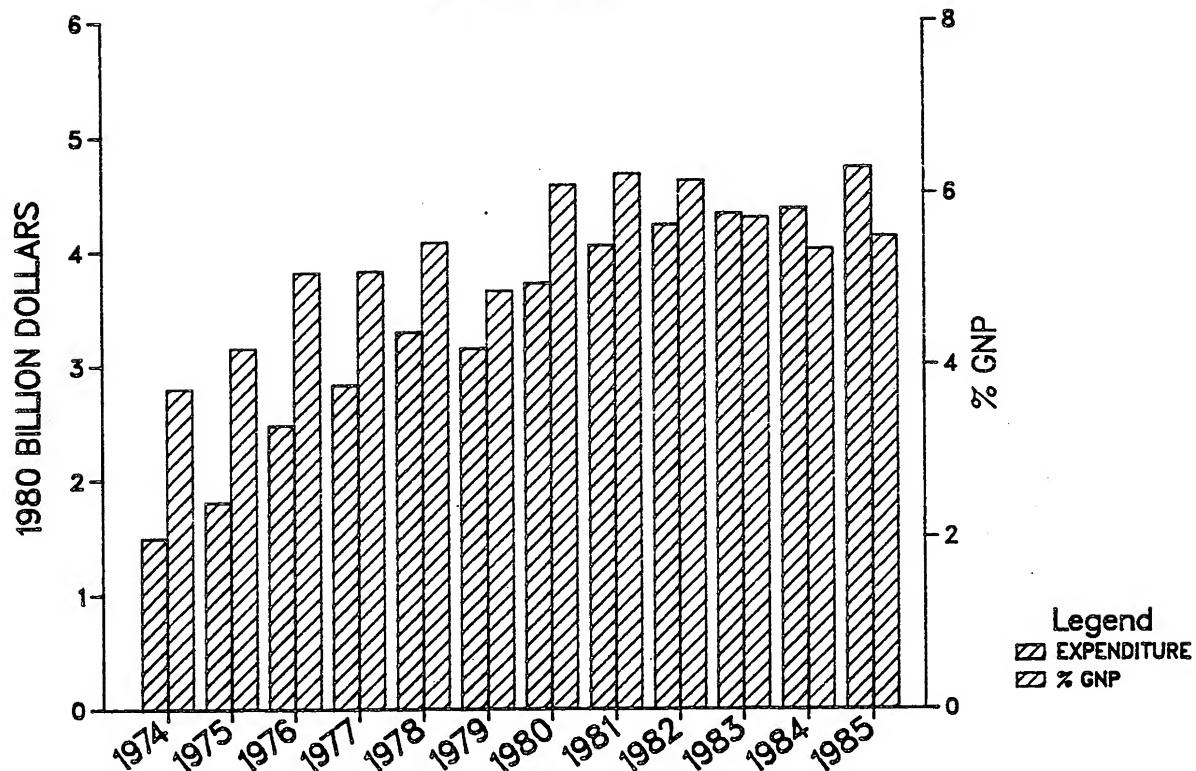
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We believe Seoul will make a serious effort to again reach the 6-percent target. Although slower economic growth next year will make the targeted ratio easier to attain in the short term, maintaining the ratio over the long term may become difficult because of declining growth in revenue. Moreover, Seoul will probably continue to seek access to IMF funds when the current arrangement expires next March. A continued agreement with the IMF will almost certainly contain a clause restricting budget deficits. The government, for its part, will probably continue to put priority on restraining inflation and slowing growth of foreign debt. These considerations will tend to make Seoul wary of increasing overall government spending, including that for defense. [redacted]

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REPUBLIC OF KOREA
REAL DEFENSE EXPENDITURES
1974 TO 1985



Data for 1984-85 is estimated

Legend
EXPENDITURE
% GNP

TABLE
COMPARISON OF DEFENSE SPENDING AS A
PERCENTAGE OF GNP
USING THE OLD AND NEW CALCULATIONS OF GNP

	<u>Old Series</u>	<u>New Series</u>
1984	4.0%	3.7%
1975	4.5	4.2
1976	5.3	5.1
1977	5.6	5.2
1978	5.6	5.4
1979	5.3	4.9
1980	6.6	6.1
1981	6.4	6.2
1982	6.6	6.2
1983	6.5	5.7
1984	6.0	5.4
1985	N/A	5.5

*Data for 1984-1985 are estimated.